

ST 06-10

Tax Type: Sales Tax

Issue: Exemption From Tax (Charitable Or Other Exempt Types)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

**ABC CLUB,
Taxpayer
v.**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

Docket # 00-ST-0000

**Denial of a sales tax
exemption number**

RECOMMENDATION FOR DISPOSITION

Appearances: Mr. Kevin Sullivan, Sauter, Sullivan and Evans for ABC Club; Mr. Kent R. Steinkamp, Special Assistant Attorney General for the Illinois Department of Revenue

Synopsis:

The Illinois Department of Revenue (hereinafter referred to as the “Department”) denied the second request of ABC Club (hereinafter referred to as the “Taxpayer” or “ABC”) for an exemption identification number which would allow the Taxpayer to purchase tangible personal property at retail free from the imposition of tax under the Illinois Retailers’ Occupation Tax Act and the Illinois Use Tax Act. The Taxpayer protested the denial and an evidentiary hearing was held during which the issue presented was whether Taxpayer is organized as a charitable not-for-profit organization as envisioned under Section 3-5(4) of the Illinois Use Tax Act (35 ILCS 105/3-5(4)) and the corresponding exemption Section 2-5(11) of the Retailers’ Occupation Tax Act (35 ILCS 120/2-5(11)). After a thorough review of the record, it is recommended that the requested exemption be denied. In support thereof, I make the following

findings of fact and conclusions of law in accordance with the requirements of Section 100/10-50 of the Administrative Procedure Act (5 ILCS 100/10-50).

FINDINGS OF FACT:

1. Taxpayer is a Missouri nonprofit corporation. Articles of Amendment were filed with the Missouri Secretary of State on January 4, 1999 stating:

The purpose for which the Corporation is organized and operated are exclusively charitable, educational, and scientific within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the “Code”)(all references to the Code herein shall also include the corresponding provision of any future United States Internal Revenue Law and the regulations promulgated thereunder). The purposes for which the Corporation is organized include, but are not limited to, raise funds and receive gifts and grants, and to use such funds, gifts and grants for its proper purposes, or to make distributions thereof for purposes and activities that qualify as exempt under Code Section 501(c)(3).

Nothing herein shall be construed to give the Corporation any purpose that is not permitted under Code Section 501(c)(3). In furtherance of its permitted purposes, the corporation may exercise any, all and every lawful power or activity which a corporation organized under the Act may exercise or transact. (Dept. Ex. No. 1; Taxpayer’s Ex. A)

2. ABC is a service organization, chartered in 1912. It operates throughout the United States and in several foreign countries. It is an acronym for **SER**vice **TO MAn**kind. (Tr. pp. 23-24)

3. Taxpayer¹ is the St. Louis chapter of ABC and was chartered in 1968. (Tr. p. 24)

4. There is no evidence of record that the ABC or ABC organizations have received exemptions from the payment of Federal Income Tax pursuant to a determination that they are 501(c)(3) organizations under the Internal Revenue Code.

5. The ABC Club Constitution states:

¹ The Taxpayer tends to use the names ABC and ABC interchangeably.

The objects and purposes for which this Club is formed are:

- To promote acquaintance, friendship and fellowship as an opportunity for service.
- To encourage and foster the idea of service and to provide opportunity for its Members to be of service to youth, to the less fortunate and the community.
- To create higher business and civic principles and to promote cooperation in all business and civic affairs.
- To provide recognition of all worthy classifications of business, professions and other fields of endeavor as dignified occupations, worthy of serving mankind.
- To provide, through its Club meetings, opportunities for the full and free discussion of matters of public interest.
- To promote, in every way, the freedom of individuals and the maintenance of the principles of free enterprise; to encourage good government and good citizenship; and to further mutual tolerance and understanding among all people. (Dept. Ex. No. 1)

6. The ABC Club Constitution - **ARTICLE V** - Membership states:

Section 1. Business or Professional Classification. Membership in this Club **may** be classified as to business or profession, which classification **may** be protected by a classification committee under the direction of the Board of Directors, and no change in any classification may be made except by authority of the Board.

Note: One of the three following alternatives **may** be adopted by the Club with respect to classification. Mark out those not adopted.

A. There shall be only one Active Member in any one classification at the same time.

B. There shall be not more than two Active Members in any one classification at the same time, and the second membership in any classification shall not be granted without the consent of the Member currently holding such classification.

C. There shall be not more than ten percent of the Active Membership in any one classification at the same time.

Section 2. Types of Membership. Membership shall be divided

into seven types:

A. Active; B. Senior-Active; C. Associate; D. Reserve; E. Military; F. Honorary and G. Corporate. (all emphasis in the original) (Dept. Ex. No. 1)²

7. The constitution states that the board of directors votes to accept or reject prospective members. In the event of a disagreement in the board of directors as to the admission of an applicant for membership, upon the request of two members of the board, a vote of the club is taken on the question of admission of the prospective member. An affirmative vote of 2/3 of the members present is required to elect that applicant to membership. (Dept. Ex. No. 1)

8. An active member who has been a member of any ABC Club for twenty (20) years or more, or who is of the age of fifty-five (55) or more years, after having been a member of one or more ABC Clubs for the last preceding five (5) or more years, who shall have retired from active business, institutional, agricultural or professional life may be elected a senior-active member upon written application to the secretary and approval of the board of directors. A senior-active member has the rights privileges and responsibilities of an active member except the senior-active member is not considered to represent any business, institutional, agricultural or professional classification and the classification that the member formerly held is open. (Dept. Ex. No. 1)

9. For each active member, an associate membership in that classification may be established. Any employee of the firm, member of the partnership or other business or professional associate of an active member, on the recommendation of such active member may, upon the recommendation of the active member, and approval of the board of directors, be

² It is evident that Taxpayer did not submit a copy of the entire Constitution. Section 9 follows Section 3. The page or pages containing information about the remainder of Section 3 - **Qualification of Members** to Section 9 - **Voting by Club on Application** were not included in the exhibit.

elected to associate membership. An associate member has all the qualifications of an active member, pays dues, may not hold office and may only vote in the absence of the active member.

(Dept. Ex. No. 1)

10. The Code of Ethics for the ABC Club states:

I AFFIRM MY ALLEGIANCE to God and my country. I believe in the everlasting endurance of my country through law and order.

I BELIEVE IN THE ABC CLUB and its principles of cooperation, friendship and mutual helpfulness.

I PLEDGE MYSELF as follows: To realize that I am a business or professional person ambitious to succeed, but that I am first an ethical person and wish no success that is not founded on the highest justice and morality. To use my greatest endeavor to elevate the standard of the calling in which I am engaged and to conduct myself in such a way that others may find it wise, profitable and conducive to happiness to follow my example. To understand that one of the greatest assets of the business or professional person is friendship and that true friends demand nothing of one another. To abuse the confidence of friendship is unethical and not in keeping with the principles of true cooperation, as adhered to by ABC International.

THE ABC CLUB EXISTS FOR THE HIGH AND NOBLE PURPOSE of benefiting mankind at large. True ABC spirit is not competitive. All real ABCns live up to the belief that true cooperation is not confined to the limits of the ABC Club but should extend to the limits of all persons.

THE EMBLEM IS A BADGE OF TRUE FELLOWSHIP, ASSISTANCE AND FRIENDSHIP, and will always stand as an ever-present reminder of the great strength of those united, and the frail weakness of the separated. The Roman fasces³ recalls the ancient lesson of the bundle of branches which was impossible to break when bound together, but was easily destroyed when separated. It is the hope that ABC Clubs be bound closely together in the spirit of cooperation, fellowship and good will in ABC International, that they will be an unbreakable power for good, advancement, helpfulness and strength in every community.

³ "A bundle of rods having among them an ax with the blade projecting, borne before Roman magistrates as a badge of authority in ancient Rome." *Webster's Third New International Dictionary*

FINALLY, I BELIEVE THAT THE DIGNITY AND CHARACTER OF INDUSTRY CAN BE SUSTAINED and improved by ABC International, to which I fully pledge my support, and will so administer my affairs to reflect credit on this great organization. (all emphasis in the original) (Dept. Ex. No. 1)

11. ABC International's mission statement is:

ABC exists for the high and noble purpose of SERVICE to Mankind by communication of thoughts, ideas and concepts to accelerate human progress in health, education, freedom and democracy. (Dept. Ex. No. 1)

12. ABC Club by-laws state that the meetings are held every 2nd and 4th Monday at 6:30 p.m. The admission fee is \$10 for active members and quarterly dues of all members is \$15. International and District dues are payable in accordance with the constitution and by-laws of ABC International. The membership dues are sent to ABC International which is responsible for communicating with members with a quarterly newspaper. ABC International also provides insurance to the members for ABC activities. (Dept. Ex. No. 1; Tr. p. 39)

13. A candidate for ABC is invited to attend an orientation and given an opportunity to see if the person is comfortable with its activities. The organization has about 40 members with 18-20 active in its events. Meetings are held once a month. Businesses are not members of ABC. (Tr. pp. 82-84)

14. One of the benefits of being a member of ABC is getting to know people in different professions. An example was given of a person owning a brake and muffler shop and being able to trust that person with work that needs to be done. (Tr. pp. 87-88)

15. Article IV entitled "Funds and Disbursements" of the "ABC CLUB BY-LAWS" states:

Section 1. Two Funds. The monies of the club shall be deposited in two funds which shall be kept separate and accounted for separately. The first shall be the General Fund, into which dues and fees shall be paid by members, and from which disbursements

shall be made for the general operating expenses of the club.

The second fund shall be the Sponsorship Fund, into which shall be deposited the income from such events and activities as are carried on for charitable and sponsorship purposes, and from which disbursements shall be made solely for such sponsorship and charitable purposes. (Dept. Ex. No. 1)

16. According to the by-laws the standing committees are: (1) Membership, (2) Eligibility and classification, (3) Program, (4) Sponsorship, (5) Extension, (6) Inter-Club Relations, (7) Attendance, (8) Reception, (9) Social, (10) Publicity, (11) Sick and Visitation, (12) Ways and Means, and (13) Bingo. (Dept. Ex. No. 1)

17. ABC International Sponsorship Fund ABC to the West 10637 is exempt from Federal Income Tax under “Group Ruling Number 3134, section 501(c)(3) of the Internal Revenue Code.” The exemption was granted in January 1979.⁴ (Dept. Ex. No. 1)

18. The Taxpayer owns and operates a 108-unit apartment complex for low-income tenants in Anywhere, Illinois.⁵ It acquired the property in April 1999 by a donation from the prior for-profit owner. (Taxpayer’s Ex. F; Tr. pp. 11-17, 41-43)

19. When the Taxpayer acquired the property, it had only 70% occupancy. By July 31, 2005, the occupancy had risen to 95.4%. (Taxpayer’s Ex. G; Tr. pp. 50-51)

20. The rent of the tenants that live in the complex are subsidized by a Housing Assistance Payment (hereinafter referred to as “HAP”) contract with the U.S. Department of Housing and Urban Development (hereinafter referred to as “HUD”). HAP payments are supplemental government payments. The amount of rent that the tenant pays plus the amount that the owner receives from the government is intended to be sufficient to cover all the costs of the ownership and maintenance of the real estate. (Taxpayer’s Ex. F; Tr. pp. 11-20)

⁴ There is no evidence of record that this Taxpayer places money directly into or removes money from this fund.

⁵ The Department denied ABC’s request for a property tax exemption for the Manor. That matter is in review in administrative proceedings.

21. The average age of a tenant in Manor is 20 with the range of ages from 1 through 68. The average number of residents is 3-per apartment. (Taxpayer's Ex. H; Tr. pp. 51-53)

22. The Taxpayer's divisional statement of financial position for August 31, 2002 states that the club had total liabilities and net assets of \$261,329⁶; Manor had total liabilities and net assets of \$2,824,661⁷, for a total of \$3,085,900. (Dept. Ex. No. 1)

23. The Taxpayer's divisional statements of financial position for August 31, 2003 states that the club had total liabilities and net assets of \$286,050⁸, Manor had total liabilities and net assets of \$2,694,048⁹ for total liabilities and net assets for that year of \$2,980,097. (Dept. Ex. No. 1)

24. ABC's divisional statements of activities for the years ended August 31, 2002 and 2003 and its financial statement¹⁰ for the same period show that in 2002 ABC's net assets at the beginning of the year for the club were \$257,340 and at the end of the year were \$255,998. For Manor the net assets at the beginning of the 2002-year were \$2,645,781 and at the end of the year they were \$2,588,719. Total net assets at the beginning of the 2002-year were \$2,903,121 and at the end of the year that amount was \$2,844,171. For 2003, net assets at the beginning of the year for the club were \$255,998 and at the end of the year were \$281,492. For Manor, net assets at the beginning of the year were \$2,588,719 and that amount at the end of the year was \$2,451,779. The total net assets for 2003 for the beginning of the year is \$2,844,717 and at the end of the year \$2,733,271. (Dept. Ex. No. 1; Taxpayer's Ex. C)

⁶ Of this amount, cash accounted for \$44,518, preferred stock was \$149,771, and mutual funds were \$39,692.

⁷ Of this amount, property and equipment, including land and building, accounted for \$3,114,993 less accumulated depreciation and other factors.

⁸ Of this amount, cash accounted for \$57,201 and the preferred stock amount is \$221,810.

⁹ Of this amount, land and building accounted for \$3,121,518, less accumulated depreciation and other factors.

¹⁰ The testimony of the "director of programs and director of finance with regard to the ABC project" (Tr. p. 30) was that the finance statements (Taxpayer's Ex. C, D) were audited. (Tr. p. 60) However, both exhibits started on page four, did not supply the name of the auditor, and did not contain the Notes to the Financial Statements, which according to the documents "are an integral part of this statement." The categories in the finance statements are arranged differently than those in the divisional statement of activities.

25. Taxpayer's "Statement of Activities for the year ended August 31, 2003" shows total unrestricted revenue, support and reclassifications of \$1,386,925, total temporarily restricted revenue, support and reclassifications of \$5,600 for total revenue support and reclassifications of \$1,392,525. Total unrestricted and restricted expenses were \$1,503,971. The unrestricted changes in net assets were (\$117,046); temporarily restricted changes in net assets were \$5,600, for a total of (\$111,446). Unrestricted net assets at the beginning of the year were \$2,628,100; restricted net assets at the beginning of the year were \$216,617 for total net assets at the beginning of the year of \$2,844,717. At the end of the 2003 fiscal year, ABC had unrestricted net assets of \$2,511,054; temporarily restricted assets of \$222,217 for total net assets at the end of the 2003 fiscal year of \$2,733,271. (Taxpayer's Ex. C, D)

26. Taxpayer's "Statements of Cash Flows for the 10-month period ending June 30, 2004 and year ended August 31, 2004" [sic]¹¹ state:

	<u>2004</u>	<u>2003</u>
Cash Flows from Operating Activities		
Membership receipts	\$ 1,585	\$ 3,933
Rental receipts	499,036	499,802
Fundraising receipts	6,907	5,057
Bingo receipts	668,143	845,866
Public support receipts	845	3,368
Investment receipts	15,090	18,458
Cash paid for membership services	(3,620)	(4,034)
Cash paid for rental activities	(458,372)	(523,445)
Cash paid for fundraising	(3,081)	(3,990)
Cash paid for bingo operations	(571,663)	(708,148)
Cash paid for other program expenses	(39,729)	(39,326)
Cash paid for sponsorship	(61,546)	(87,205)
Cash paid for management and general expenses	<u>(8,681)</u>	<u>(10,208)</u>
Net Cash provided by Operating Activities*	<u>44,914</u>	<u>128</u>
Cash Flows from Investing Activities		
Deposits in other funded reserves	(4,378)	—
Withdrawal of other funded reserves	-	6,669

¹¹ The date should be August 31, 2003.

Purchase of fixed assets	-	(6,524)
Proceeds from sale of short-term investments	185,052	58,350
Purchase of short-term investments	(199,441)	(61,618)
Net Cash Used by Financing Activities	(18,767)	(3,123)
Cash Flows from Financing Activities		
Repayment of long-term debt	<u>(2,862)</u>	<u>(1,677)</u>
Net Cash Used by Financing Activities	<u>(2,862)</u>	<u>(1,677)</u>
Net Increase (Decrease) in Cash	23,285	(4,672)
Cash – Beginning of Year	<u>59,613</u>	<u>64,285</u>
Cash – End of Year	\$ <u>82,898</u>	\$ <u>59,613</u>
*Cash Flows from Operating Activities		
Change in Net Assets	\$ (56,976)	\$ (111,446)
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation	94,258	113,247
Realized loss on sale of investments	8,979	6,751
Unrealized loss (gain) on investments	13,506	(16,802)
Change in assets – (increase) decrease		
Accounts receivable	(1,887)	110
Interest receivable	(1,545)	-
Prepaid expenses	(11,218)	2
Other assets	(10,046)	889
Change in liabilities – increase (decrease)		
Accounts payable	(4,579)	9,533
Accrued payroll	13,125	(1,656)
Tenant security deposits	<u>1,297</u>	<u>(500)</u>
Total Adjustments	<u>101,890</u>	<u>111,574</u>
Net Cash Provided by Operating Activities	\$ <u>44,914</u>	<u>128</u>
(Taxpayer's Ex. D)		

27. “ABC obtains its funds through a Bingo operation.” (Tr. p. 30, testimony of Mr. John Doe, previous president and chairman of the board of ABC and at the time of the hearing, director of programs and finance.) Games are held every Thursday night. Members of the Taxpayer volunteer their time for the bingo operation. The main purpose of the ABC meetings is to evaluate Taxpayer’s mechanisms for operating its bingo and pull tab games, a significant

income source for this Taxpayer. Discussions are held about staffing and improving relations with the customers, specials and other activities that the Taxpayer does, such as applications for potential sponsorships. (Tr. pp. 30, 37)

28. Some of the Taxpayer's income is given away to "Sponsorships." For the fiscal year ended August 31, 2003 the organization gave away \$85,170.38. For the ten-month period ending June 30, 2004, the organization gave away \$60,446. For July through December 2004, ABC gave away \$23,155. For the period from January through June 30, 2005 the organization gave away \$21,378.79. Examples of Sponsorship organizations that ABC gave money to are: Lambda Beta Lambda,¹² Feed My People, St. Louis VAMC, Friends of Kids With Cancer, 100 Neediest Cases, Independence Center, Pregnancy Resource Centers, St. Mary High School, St. Louis Veterans Home, Mary Culver Home,¹³ YEHS Senior Center,¹⁴ James S. McDonnell USO, Sunshine Ministries, MDA, Employment Connection, People To People Relief Society, South Ministry Presbyterian Church, El-Ritiro, Salvation Army, Crestwood Elks, Asst. League of St. Louis, St. Louis Metro Athletics, Bevo Area Comm. Improv., Sunshine Ministries, MVH Assistance League, Doris Davis helping Hand Shelter, 5 Church Older Adult Center, F.U.R.R.Y., C.C.B.F. Inc., Our Lady of Providence Parish, Affton Americans, and World Aquarium. All are located in Missouri except for Doris Davis Helping Hand Shelter located in East St. Louis, Illinois, which was given \$2,000 in 2004. (Taxpayer's Ex. E; Tr. pp. 34-35)

29. As of January 1, 2004, ABC adopted a resolution regarding Manor. The resolution added Article XII to the by-laws and states:

Notwithstanding any rental agreement provisions to the contrary, it shall be the Corporation's policy in owning, managing, and operating its multi-family housing development located in

¹² There was a relationship to a club officer in 2004. In the exhibit it is spelled both Lamda and Lambda.

¹³ There is a relationship with an employee.

¹⁴ There was a relationship with a council member in 2003.

Anywhere, Illinois, known as Manor not to evict a tenant solely for non-payment of rent or other charges due under the rental agreement, or in connection with the operation of Manor, if such non-payment is due to said tenant's documented financial inability to pay said rent or other charges. This provision shall not be construed to prohibit the Corporation from evicting tenants in accordance with the terms of their leases for, among other things, failure to pay for reasons other than their financial [ina]¹⁵bility to pay rent.

It shall be the Corporation's policy in owning, managing, and operating Manor, not [to] [i]mpose fees associated with accepting and processing applications, screening applicants, or verifying [inc]ome eligibility on any applicant, and not to impose other fees, including security deposits, pet [dep]osits, meal program fees, fees for supportive service programming, and late fees, on a[n] applicant or [ten]ant without income, welfare or other governmental assistance, if said tenant has a documented [fin]ancial inability to pay said fees. (Taxpayer's Ex. K; Tr. pp. 67-69)

CONCLUSIONS OF LAW:

The Retailers' Occupation Tax Act and Use Tax Act (hereinafter collectively referred to as the "Acts") impose taxes in the State of Illinois. The Use Tax Act (35 **ILCS** 105/1 *et seq.*) imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. (35 **ILCS** 105/3) The Retailers' Occupation Tax Act (35 **ILCS** 120/1 *et seq.*) imposes a tax on persons engaged in the business of selling at retail tangible personal property. (35 **ILCS** 120/2) Sections 2-5 and 3-5 of the Acts provide a list of exemptions from taxation. (35 **ILCS** 105/2-5; 35 **ILCS** 120/3-5)

At issue is Taxpayer's request for a charitable exemption from the Acts, pursuant to 35 **ILCS** 105/3-5(4) and 35 **ILCS** 120/2-5(11). Those sections of the statute state that the use or sale of tangible personal property is exempt from the tax imposed by the Acts if the personal

¹⁵ The exhibit was a bad copy of the resolution with parts of words missing. The insertion letters contained in the brackets are reasonable additions.

property is purchased by a governmental body, or by a corporation, society, association, foundation, or institution organized and operated exclusively for charitable, religious, or educational purposes. On and after July 1, 1987 no entity otherwise eligible for this exemption shall make tax-free purchases unless it has an active exemption identification number issued by the Department. 35 ILCS 105/3-5(4); 35 ILCS 120/2-5(11).

Taxpayer requested that it be issued an exemption number pursuant to the statutory provisions contained herein. The Department denied the request on the basis that Taxpayer did not demonstrate that it operates for exclusively charitable purposes. (Dept. Ex. No. 1) The Department's denial of a Taxpayer's claim for an exemption identification number is presumed to be correct, and a taxpayer has the burden of clearly and conclusively proving its entitlement to the exemption. Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455, 459 (2nd Dist. 1995); Clark Oil & Refining Corp. v. Johnson, 154 Ill. App 3d 773, 783 (4th Dist. 1987). To prove its case, a taxpayer must present more than its testimony denying the Department's determination. Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4th Dist. 1990). Rather, a taxpayer must present sufficient documentary evidence to support its claim. *Id.*

Although it was a case concerning a property tax exemption, Illinois courts have found it appropriate to use the guidelines set forth in Methodist Old Peoples Home v. Korzen, 39 Ill. 2d 149 (1968) to determine whether an entity qualifies as one organized and operated for charitable purposes for use and sales tax purposes. Wyndemere Retirement Community, *supra*; Friends of Israel Defense Forces v. Department of Revenue, 315 Ill. App. 3d 298, 303-304 (1st Dist. 2000).

In determining what is charitable use of property, courts consider the following factors:

1. Whether the benefits derived from the property are for an indefinite number of persons;

2. Whether the property benefits the public in such a way as to persuade them to an educational or religious conviction, for their general welfare;
3. Whether the property benefits the public in such a way that it reduces the burdens of government;
4. Whether the organization has no capital, capital stock, or shareholders and earns no profits or dividends;
5. Whether the organization's funds are derived mainly from public and private charity;
6. Whether such funds are held in trust for the objects and purposes expressed in the organization's charter;
7. Whether the organization dispenses charity to all that need and apply for it;
8. Whether the organization provides gain or profit in a private sense to any person connected with it;
9. Whether the organization places obstacles of any character in the way of those who need and would avail themselves of the charitable benefits dispensed; and
10. Whether the exclusively (primary) use of its property is for charitable purposes. Methodist Old Peoples Home v. Korzen, *supra*, at 156-57.

These factors are not requirements, but are guidelines that are considered in assessing an organization's charitable status. Du Page County Board of Review v. Joint Commission on Accreditation of Healthcare Organizations, 274 Ill. App. 3d 461, 468 (2nd Dist. 1995) (*leave to appeal denied*, 164 Ill. 2d 561)

As one of the guidelines enumerated in Methodist Old Peoples Home v. Korzen, *supra*, is whether a taxpayer's funds come from public or private charity, the analysis of the source of a taxpayer's funding is appropriate. ABC obtains the majority of its revenues through its bingo operations, pull tab games, rents and membership dues. In each of these situations, the people

are giving money to the Taxpayer in return for a definite benefit - i.e. the games of chance offer the possibility of financial reward, rents are payments for leasehold rights and membership dues result in membership benefits. These are not public and private charity which would be given without expectation of return compensation or added benefits as envisioned under the guidelines set forth in Methodist Old Peoples Home v. Korzen, *supra*. True charity is conducted, not for profit, but for the welfare of others.

According to the financial information submitted, in particular Taxpayer's Exhibit E, as of August 31, 2003, Lambda Beta Lambda received \$31,299.38 out of the \$85,170.38 amount given away for "Sponsorships"; as of June 30, 2004 Lambda Beta Lambda received \$20,500 out of the \$60,446 given away; from July through December 2004, Lambda Beta Lambda received \$12,000 out of the \$20,000 given away; and from January through June 2005 Lambda Beta Lambda received \$8,200 out of \$21,378.79 given away. ABC did not explain what Lambda Beta Lambda is and what its connection is with that entity, other than the evidence that a club officer had a relationship with that organization. There was no information given about the charitable nature of the entities that they give sponsorship money to. Likewise, there is really no evidence of record that money is given to charitable organizations, nor how the recipients of the sponsorships are chosen or what those entities do. Taxpayer submitted, to the Department, a listing of community services supported by ABC including human service, support for other agencies, community projects, holiday/recreational activities and fundraisers. (Dept. Ex. No. 1) Taxpayer did not testify about or explain the list.

Further, taxpayer receives substantial income from Manor Apartments, which it owns and operates. This property is a subsidized HUD Section 8 housing project. Housing assistance payments from the government plus the amount of rent a tenant pays are intended to be sufficient

to cover the costs of ownership and maintenance of the real estate. There is no indication that ABC is not receiving market value for the housing and no indication that they are running Manor at a deficit. Taxpayer offered no manual or brochure as evidence regarding the process a prospective tenant goes through when it contacts ABC about renting an apartment. What is the routine? What forms must be filled out?

Taxpayer produced a 2004 amendment to its by-laws regarding Manor that states that it is ABC's policy not to evict a tenant solely for the non-payment of rent or related charges due to the tenant's inability to pay such costs. However, ABC failed to show how that provision is implemented. From the financial information submitted for 2002 and 2003, there is no evidence that manor operated at a deficit, and in fact appears to make a profit. In addition, Taxpayer's exhibit "D", the statements of cash flows for the 10-month period ended June 30, 2004 and year ended August 31, 2003 show a much larger amount of cash on hand at the end of the 10-month period ending June 30, 2004 than the cash Taxpayer had on hand at the end of August 31, 2003. Because of the lack of evidence submitted by this Taxpayer, I cannot conclude that the by-laws were implemented with a result that the Taxpayer provided any charity.

Taxpayer's Exhibit G, entitled "Salient Facts Concerning the Manor Apartments 31-Jul-05", shows that 17 tenants were evicted from Manor Apartments for "behavioral reasons". What Taxpayer considers behavioral reasons was not explained. (Tr. pp. 49-56)

Taxpayer's Exhibits G and I, entitled "Rent Due By Unit for July, 2005 for Manor", discuss the capacity of the tenants to pay their rent portions. In neither of the documents does ABC discuss the fact that the \$0 rent paid by some of the tenants is supplemented by government payments. In other words, the self-serving documents prepared by ABC and submitted as exhibits G and I are not factual as to the amount of rents received by ABC for the units.

In addition, in Exhibit I, which shows that 6.67% was the total rent paid by tenants, the testimony was that the write-off figures for the exhibit were taken from the financial statements. (Tr. p. 62) As ABC did not submit the first three pages of the financial statements, the name of the auditor, and did not include the notes to the financial statements which are essential to the understanding of any financial statements, I have a problem with the credibility of all the financial statements submitted and any extrapolation of those documents done by the Taxpayer.

ABC had the Executive Director of the Anywhere Housing Authority, a government corporation, testify that Manor is a similar housing program to other government projects served through the Housing Authority. The executive director agreed that “if Manor was not being operated by ABC and was not in existence it would increase the burden on his agency” and guessed that it would cost the taxpayers more money. (Tr. p. 14) Unfortunately, ABC did not have the witness elaborate how it would cost the taxpayers more money. As it is, ABC is receiving taxpayers’ money for the subsidized rents for the apartments, which certainly is not relieving any government burden.

What ABC’s financial position statements show is that Manor has substantial assets including cash, accounts receivables, tenant security deposits, replacement reserves, property¹⁶(less accumulated depreciation), work in progress, and other assets. Its liabilities include accounts payable, accrued payroll, current portion of long-term debt, tenant security deposits,¹⁷ restricted and unrestricted net assets. ABC’s assets include cash, prepaid expenses, preferred stock and mutual funds, equipment (less accumulated depreciation), bonds, and other assets.

¹⁶ Including land and the building valued at \$3,112,129 in 2002 and \$3,121,518 in 2003.

¹⁷ This amount does not agree with the tenant security deposit amount listed under assets.

As ABC failed to submit documentary evidence that the entity itself has a 501(c)(3) designation from the Internal Revenue Service, it is unclear whether or not the stock, bonds and other financial information provided are for ABC, specifically. Although there was much testimony about the fact that the Articles of Incorporation state that ABC's purpose is that it is organized as a charitable organization under 501(c)(3) of the Internal Revenue Code (Tr. pp. 26-27), the only documentary evidence submitted in regards to that assertion was a letter from the Internal Revenue Service stating that "Internal International Sponsorship Fund is exempt from Federal Income Tax under Group Ruling Number 3134." The letter was addressed to ABC International Sponsorship Fund ABC with a St. Louis, Missouri address. The address and name are not the same as the Applicant herein.

It is also appropriate to analyze the articles of incorporation, charter and constitution of a taxpayer to see how they help explain or highlight a taxpayer's asserted charitable purpose. The Amended and Restated Articles of Incorporation for ABC state that it is organized for charitable, educational and scientific purposes within §501(c)(3) of the Internal Revenue Code and to raise funds and receive gifts and grants and to use those for activities that qualify as exempt under §501(c)(3). ABC International Sponsorship Fund ABC to the West 10637 is exempt from the imposition of federal income tax under §501(c)(3) of the Internal Revenue Code. Based upon that, I can conclude that the fund has no capital, capital stock, or shareholders. However, the fund is not the Taxpayer herein. The Taxpayer failed to provide a connection between the fund and ABC. How the Taxpayer operates and functions viz-à-viz the fund is unclear from the evidence provided. There is nothing in the record to establish that either the ABC or ABC organization is exempt from federal taxation.

In addition, there was nothing in ABC's financial information submitted to show that the monies of the club were deposited into the two separate funds mandated by the ABC Club by-laws. There was no indication of a segregation into a General Fund and a Sponsorship Fund.

In actions by corporations to have real estate declared exempt from taxation for certain years on the grounds that it is a charitable corporation, the Illinois Supreme Court has held that the certificate of incorporation is the controlling evidence of the purpose for which the organization was created. Oak Park Club v. Lindheimer, 369 Ill. 462 (1938) It is well settled in Illinois that the character and purpose for which a corporation is organized must be ascertained from its Articles of Incorporation. People v. Wyanett Light Co., 306 Ill. 377 (1922); Rotary International v. Paschen, 14 Ill. 2d 480 (1958) The standards for membership found in the ABC Club Constitution state that the classification for membership is open to a professional or business person. Based upon the record herein, the ABC Constitution and by-laws control ABC, and in fact the record establishes that the Taxpayer uses the ABC and ABC names interchangeably. Because of the restrictions that limit the numbers of people in a business or professional classification, it can't be said that the membership is open to all who might wish to avail themselves of any benefits dispensed. It has also not been established that there is a fee waiver policy if a person can not afford the membership dues for ABC. In other words, it also cannot be said that the benefits are derived for an indefinite number of persons, a guideline of Methodist Old Peoples Home v. Korzen, *supra*.

Although it was asserted that ABC doesn't blackball people (Tr. p. 82), the ABC Club Constitution allows the board of directors to accept or reject prospective members and even has a provision for a vote of the club in case there is a disagreement at the board level regarding the acceptance of a prospective member. (Dept. Ex. No. 1) This is another restriction on membership that shows the organization is not available to an indefinite number of persons.

ABC is an organization of persons who have joined together to promote higher business and civic principles and to encourage service within the community. The membership qualifications, according to the ABC Club Constitution, restrict members to those involved in a business or profession. 86 Admin. Code ch. I Sec 130.2005 (g) addresses the sales tax exemption possibility of "Nonprofit Professional and Trade Associations – Labor Unions – Civic Clubs – Patriotic Organizations." It states:

Nonprofit Bar Associations, Medical Associations, Lions Clubs, Rotary Clubs, Chambers of Commerce and other professional, trade or business associations and labor unions, which draw their funds largely from their own members, and as to which an important purpose is to protect and advance the interests of their members in the business world, are not organized and operated exclusively for charitable or educational purposes even though such organizations may engage in some charitable and educational work. . .

In Rotary International v. Paschen, 14 Ill. 2d 480 (1958), the court found that an administrative and coordinating body for various Rotary clubs throughout the world, having as its objective encouraging and fostering ideals of service to local communities, was not a charitable organization using the property for charitable purposes under the property tax code. The court said that objectives of a not-for-profit corporation may be commendable, yet not charitable under the law. *Id.* at 488-89 The object of Rotary is to encourage and foster the ideal of service as the basis of worthy enterprise, to encourage and foster the development of

acquaintances as an opportunity to serve, to set high ethical standards in businesses and professions, and to recognize Rotarians in their businesses as an opportunity to serve society and advance good will and peace through a world fellowship of business and professional men. *Id.* at 482. The evidence of record establishes that ABC and ABC are structured pursuant to these same principles.

The Illinois Supreme Court also determined that another entity with a structure and ideals similar to those of ABC was not a charitable organization in Kiwanis International v. Lorenz, 23 Ill. 2d 141 (1961). Citing Rotary International v. Paschen, *supra*, the court said that the record established that the promotion by business and professional men of the spirit of fraternalism among members, providing practical means to form enduring friendships, exchanging experiences and improving the member's leadership in the community was laudable. However, the social professional and business advancement of the members and the element of personal advantage to those members is not what is contemplated as being charitable. Kiwanis International v. Lorenz, *supra*, at 146

The well-settled law in Illinois regarding taxation exemption is that a statute granting exemption must be strictly construed in favor of taxation and against exemption. Wyndemere Retirement Community v. Department of Revenue, *supra*, at 459. Further, the exemption claimant has the burden of proving its entitlement clearly and conclusively with all facts construed and debatable questions resolved in favor of taxation. *Id.*

The Taxpayer has shown that it does not meet the majority of the guidelines set forth in Methodist Old Peoples Home v. Korzen, *supra*, and has not established that it is a charitable organization. I am not persuaded that the Taxpayer's activities, however meritorious, should be

subsidized by the people's tax dollars. I therefore recommend that the denial of tax-exempt status to ABC be sustained.

Barbara S. Rowe
Administrative Law Judge
Date: June 7, 2006